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ABSTRACT

This study evaluates the effects of the Minnesota education expense tax deduction law. The study design was limited, since the Minnesota Department of Revenue declined to participate in the survey. Within these limitations the study looked at (1) the number of tax returns claiming education deductions, (2) the distribution of gross income for those returns with dependent education expense deductions in comparison with those returns that list dependents but claim no dependent education deductions, and (3) the relationship between number and amount of deduction and access to nonpublic education. Findings include: (1) a small but growing number of returns are claiming educational deductions; (2) in 1980 more public school parents and small families were taking advantage of the law; and (3) correlations indicate a strong relationship between income and claiming the deduction. The available data provide no indication of the type of expenditures the deductions pay for, the institutional benefits public or nonpublic schools receive, or the benefits to the parents. The author ends by stating that further study is needed. (MD)

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MINNESOTA'S DEPENDENT EDUCATION EXPENSE TAX DEDUCTION LAW

by

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Minnesota's Dependent Education Expense

Tax Deduction Law

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V.L.H.

C.H.S.

Introduction

On October 4, 1982 the United States Supreme Court agreed to hear an appeal of Mueller et. al. vs Allen in which the constitutionality of the Minnesota education expense tax deduction law (M.S. 290.09 Subdivision 22) was upheld by the Eighth U.S. Circuit Court of Appeals. The Supreme Court ruling will have significant educational policy implications because 1) in Rhode Island Federation of Teachers vs. Norberg the First U.S. Circuit Court of Appeals in Boston ruled an almost identical Rhode Island tuition assistance law unconstitutional and 2) President Reagan's proposed federal income tax tuition credit raises the same constitutional issues. The purpose of the present inquiry was to identify effects of M.S. 290.09 Subd. 22.

Background of the Problem

Minnesota's first elementary/secondary tuition and transportation expense deduction law was passed in 1955 (Laws 1955 Session Chapter 741

Section 1, Item 19) allowing up to a $200 deduction per child. Inspite of several proposals, no changes were enacted until Laws 1971 Session Chapter 944 Section 290.086 Subd. 5 authorized a non-public school education cost tax credit of $50, $100, and $140 for kindergarten, elementary, and secondary students respectively. The 1971 statute was challenged and ruled unconstitutional by the Minnesota Supreme Court in Minnesota Civil Liberties Union et. al. vs State of Minnesota on November 26, 1974. In Laws 1976 Session Chapter 37 Section 290.09 Subd. 22 the present statute authorizing state income tax education expense deductions up to $500 and $700 for elementary and secondary students respectively was enacted. Expenses may include tuition, textbooks, transportation and other expenses incurred by residents in meeting compulsory attendance laws through enrollment in public or private schools in Minnesota or adjacent states. Expenses for materials used in religious instruction, worship, and extracurricular activities are specifically excluded.

The constitutionality of M.S. 290.09 Subd. 22 was challenged in Minnesota Civil Liberties Union et. al. vs Roemer et. al. The U.S. District Court, Minnesota District, Third Division ruled on June 19, 1978 that the statute was neutral, neither impeded nor advanced religious activity, and did not have the primary effect of advancing religion in violation of the First Amendment Establishment Clause. In 1979 the First U.S. Circuit Court of Appeals ruled in Rhode Island Federation of Teachers vs Norberg an almost identical statute unconstitutional. On the basis of this precedent the constitutionality of M.S. 290.09 Subd. 22 was again challenged in Mueller et. al. vs Allen. Plaintiffs used State Department of Education

enrollment data to argue that from 82 percent to 96 percent of students who pay tuition attend sectarian schools which already receive aid for textbooks, transportation, and other costs and therefore a primary effect of the statute was support and advancement of religious activity. The district trial court ruled in favor of the defendents, the Eighth United States Circuit Court upheld the trial court on April 30, 1982, and the case will now be heard by the United State Supreme Court.

Arguments of both plaintiffs and defendents indicated that there is virtually no direct evidence on the effects of the law. The present study was initiated to further inquire as to the nature of deductions claimed and who are the beneficiaries.

Study Design

Design of the study, analysis of data and findings are subject to the following limitations:

1) Deduction data are a) recorded on completed state income tax forms, b) confidential, and c) accessible only to the Minnesota Department of Revenue.

2) Because of pending litigation, the Department of Revenue declined to participate in a cooperative survey of parent/filers claiming education deductions to determine a) nature of expenses claimed, b) effect on choice of school, and c) level of satisfaction with the law.

3) Research questions addressed in the study were limited by a) access to Department of Revenue generated data from samples for 1978 and 1980, and b) confidentiality requiring that additional analyses be conducted by the Department of Revenue.

Within these limitations, objectives of the study were guided by the following general research questions:

1) How many returns (individual and joint combined) claimed education expense tax deductions under Minnesota Statute 290.09 Subdivision 22, what is the amount of deductions claimed, how much income tax revenue is foregone by the state, and what trends do data indicate?

2) What is the distribution of Minnesota Gross Incomes (MGI) for returns claiming the dependent education expense deduction and how does it compare with the distribution of MGI for returns which list dependents but do not claim dependent education expense deductions?

3) What relationship exists between number and amount of education expense deduction and access to non-public education opportunity using numbers and enrollments in non-public schools by regional Educational Cooperative Service Unit (ECSU) as proxy measures?

The population(s) studied consisted of state income tax returns filed with the Minnesota Department of Revenue and contained in a) the 1978 M-1 Income Tax Return File and b) the 1980 M-1 Income Tax Return File. The Department of Revenue drew inverse proportional random samples from each of 20 MGI stratifications of the files (N = 22,556 for 1978 and N = 20,351 for 1980). Validity of inferences from sample data were assessed by comparison with four known population parameters in nine MGI stratifications and totals for both sample years. While the percent difference was -1.11 percent in the largest gross loss stratifications in 1978, differences in most stratifications for that year and for all stratifications during 1980 were typically less than plus or minus one percent. The Department of

Revenue estimated amounts of income tax revenue forgone by the state by multiplying the marginal tax rate for all itemizers, 12.8 percent, times the estimated deductions for the population(s).

Findings

The data in Table 1 respond to Research Question #1. The number of returns on which the dependent education expense deduction was claimed increased 161 percent from an estimated 33,050 in 1978 to 86,180 in 1980. Amount of deductions rose 66 percent from $19,268,489 in 1978 to $31,990,824 in 1980 and income tax revenue forgone by the state increased from an estimated $2,466,366 in 1978 to $4,094,825 in 1980.

The Department of Revenue generated a frequency distribution of dependent education expense deductions in $100 increments with population estimates of numbers of returns filed, dependents claimed, and MGI associated with each $100 increment for both years. Data in Table 2 indicate that from 1978 to 1980 a larger proportion of itemized returns tended to claim smaller dependent education expense deductions. In 1978 for example, 50 percent of the tax returns had deductions of $500 or less. In 1980, 50 percent of the returns had deductions of $200 or less. The mean number of dependents per return in 1980 was 2.38 whereas in 1978 it was 2.71 dependents per return. Returns claiming dependent education deductions of $600 or less accounted for 52 percent of MGI represented on returns claiming the deduction in 1978. In 1980, returns claiming dependent education deductions of $300 or less accounted for 54 percent of MGI represented on returns claiming the deduction.

The columns for MGI in 1978 and 1980 in Table 2 were divided by the number of returns filed to yield mean income per return for each of the

Table 1

Population Estimates of Number of Returns Claiming Education Expense Deduction, Amount of Deduction, and Forgone Income Tax Collections for 1978 and 1980

	1978	1980	Change (Percent)[a]
Number of Itemized Returns	1,723,491	1,743,498	+ 1.16
Returns with Education Deduction	33,050	86,180	+160.80
Percent of Returns[a]	1.92	4.94	
Total Education Deduction	$19,268,489	$31,990,824	+ 66.03
Average Deduction per return	$583.02	$371.21	- 36.33
Standard Deviation per return	$514.04	$466.03	- 9.34
Average Deduction per Dependent[a]	$217.00	$156.00	- 28.11
Forgone Tax Collections	$2,466,366	$4,094,825	+ 66.03

[a]Computed by authors

Source: Minnesota Department of Revenue

Table 2

Sample Based Population Estimates Number of Returns, Number of Dependents, and Minnesota Gross Income Associated with Size of Education Expense Deduction in $100 Intervals for 1978 and 1980

Interval[a]	1978						1980					
	Returns		Dependents		MN Gross Income		Returns		Dependents		MN Gross Income	
	Number	%	Number	%	Amount	%	Number	%	Number	%	Amount	%
1 - 100	3,502	10.66	7,697	8.66	82,987,904	8.73	29,470	34.37	58,024	28.35	778,105,154	29.04
101 - 200	4,341	13.21	13,052	14.68	91,874,186	9.66	15,341	17.89	39,732	19.41	430,903,176	16.08
201 - 300	3,492	10.63	8,736	9.83	86,485,229	9.10	8,524	9.94	19,092	9.33	245,314,582	9.15
301 - 400	3,176	9.67	8,129	9.15	84,752,412	8.92	5,127	5.98	11,803	5.77	145,700,082	5.44
401 - 500	2,862	8.71	7,656	8.61	71,645,616	7.54	3,582	4.18	9,007	4.40	120,065,318	4.48
501 - 600	2,773	8.44	5,860	6.59	82,424,936	8.67	3,806	4.44	9,889	4.83	121,342,358	4.53
601 - 700	1,584	4.82	4,354	4.90	44,976,969	4.73	3,108	3.62	9,456	4.62	101,997,079	3.81
701 - 800	4,092	12.46	10,488	11.80	155,972,993	16.41	6,793	7.92	14,399	7.04	297,936,768	11.12
801 - 900	862	2.62	2,633	2.96	19,864,087	2.09	1,094	1.28	3,377	1.65	35,728,057	1.33
901 - 1,000	678	2.06	2,405	2.71	19,581,218	2.06	1,172	1.37	3,436	1.68	38,401,915	1.43
1,001 - 1,100	1,169	3.56	3,500	3.94	37,288,230	3.92	1,091	1.27	2,279	1.11	42,024,742	1.57
1,101 - 1,200	342	1.04	885	1.00	8,333,194	.88	556	.65	1,524	.74	20,291,881	.76
1,201 - 1,400	708	2.16	2,288	2.57	24,958,182	2.63	1,475	1.72	4,925	2.41	62,880,304	2.35
1,401 - 1,600	1,471	4.48	4,471	5.03	73,605,728	7.74	2,235	2.61	7,093	3.47	111,023,623	4.14
1,601 - 2,100	972	2.96	3,009	3.39	36,619,518	3.85	1,247	1.45	4,669	2.28	64,967,644	2.42
2,101 - 5,100	826	2.52	3,725	4.19	29,257,186	3.08	1,128	1.32	5,965	2.91	63,178,523	2.36

[a] When a $100 interval contained less than 1 percent of the number of returns in 1978 it was combined with the preceding interval.

Source: Minnesota Department of Revenue

sixteen deduction categories. For example, the MGI figure for deductions of $100 or less for 1978 was $82,987,904, the category had 3,502 returns, yielding a mean gross income of $23,697 (rounded) for each return filed. Similarly, the MGI figures in Table 2 were divided by the number of dependents in each deduction size category. For example, the $82,987,904 MGI for deductions of $100 or less divided by the 7,697 dependents in that category yielded a mean income of $10,782 per dependent. These data are presented in Table 3. While some of the fluctuations in Table 3 can not be readily explained, there is generally a much stronger relationship between the mean MGI per return and the size of deduction than the mean MGI per dependent and the size of deduction. Rank order correlations of .182 and .083 for 1978 and 1980 indicated that basically there was little if any relationship between mean MGI per deperdent and size of deduction claimed. Rank order correlations of .685 for 1978 and .9 for 1980 indicated that there was a sizable relationship between MGI/return and size of deduction. Furthermore, this relationship was much stronger in 1980 than in 1978. These data indicate that the size of the education deduction claimed was much more dependent on the income of the filer(s) than the number of dependents.

The first concern in Research Question #2 was, "In what MGI brackets do returns claiming dependent education expense deductions fall?" Data addressing this concern are the population estimates for 1980 presented in column 1 of Table 4 (similar data for 1978 were not available). The largest number of returns claiming dependent education deductions, 19,954 (23 percent) occurred in the $30,000 to $39,999 stratification and represented

Table 3

Average Minnesota Gross Income Per Dependent
and Per Return for 1978 and 1980

Deduction Size Category	1978		1980	
	Dependent	Return	Dependent	Return
1 - 100	$10,782	$23,697	$13,410	$26,403
101 - 200	7,039	21,164	10,845	28,088
201 - 300	9,900	24,767	12,849	28,779
301 - 400	10,426	26,685	12,344	28,418
401 - 500	9,358	25,034	13,330	33,519
501 - 600	14,066	29,724	12,270	31,882
601 - 700	10,330	28,395	10,786	32,818
701 - 800	14,871	38,116	20,692	43,859
801 - 900	7,544	23,044	10,580	32,658
901 - 1,000	8,142	28,881	11,176	32,766
1,001 - 1,100	10,654	31,897	18,440	38,520
1,101 - 1,200	9,416	24,365	13,315	36,496
1,201 - 1,400	10,908	35,251	12,768	42,631
1,401 - 1,600	16,463	50,037	15,653	49,675
1,601 - 2,100	12,170	37,675	13,915	52,099
2,101 - 5,100	7,854	35,420	10,592	56,010
Rank order correlation with deduction size category	.182	.685	.088	.900

Table 4

Population Estimates--Number of Returns With Dependents that Claim and Do Not Claim Dependent Education Deductions and Amount of Deduction by Minnesota Gross Income Stratification Levels for 1980

MN Gross Income Stratification	Returns				Education Deduction	
	with Deductions		without Deductions			
	Number	Percent	Number	Percent	Amount	Percent
Less than $-19,999	32	.04	2,075	.49	25,667	.08
-19,999 to -10,000	21	.02	1,074	.25	13,942	.04
- 9,999 to -1	62	.07	6,018	1.41	12,119	.04
0 to 0	0	0	175	.04	0	0
1 to 2,499	200	.23	3,199	.75	59,790	.19
2,500 to 4,999	398	.46	4,515	1.06	156,697	.49
5,000 to 9,999	2,666	3.09	24,923	5.83	653,090	2.04
10,000 to 14,999	7,421	8.61	42,519	9.94	1,856,886	5.80
15,000 to 19,999	9,180	10.65	59,669	13.95	2,132,744	6.67
20,000 to 24,999	15,782	18.31	70,715	16.53	4,512,111	14.10
25,000 to 29,999	16,160	18.75	67,837	15.86	5,710,520	17.85
30,000 to 39,999	19,954	23.15	85,309	19.95	8,800,046	27.51
40,000 to 49,999	7,468	8.67	31,071	7.26	3,123,235	9.76
50,000 to 74,999	4,183	4.85	18,540	4.33	2,423,622	7.58
75,000 to 99,999	1,127	1.31	5,154	1.20	1,147,688	3.59
100,000 to 124,999	646	.75	2,031	.47	531,672	1.66
125,000 to 149,999	337	.39	1,094	.26	299,297	.94
150,000 to 174,999	190	.22	651	.15	180,289	.56
175,000 to 199,999	99	.11	278	.06	78,558	.25
200,000 And Over	254	.29	874	.20	272,852	.85
Total	86,180	100	427,721	100	31,990,825	100

$8,800,046 in deductions. Well over half (60.2 percent) of the returns fell in the $20,000 to $39,999 MGI range representing an estimated $19,022,677 in deductions or 59 percent of the total.

The distributions by MGI stratification for returns claiming the dependent education deduction and returns with dependents but not claiming the education expense deduction were compared using 1) the percents in Table 4 and 2) a contingency table analysis. Using the percents in Table 4, the distributions tend to have a similar pattern, with larger percents of returns claiming the education deduction tending to fall in higher MGI brackets. While 60.2 percent of those claiming the deduction reported MGI's between $20,000 and $39,999, 52.3 percent of returns with dependents not claiming education expense deductions fell within the same range. About 23.2 percent of returns claiming the education deduction fell below $20,000 compared with 33.7 percent of returns with dependents but not claiming the deduction. At the $40,000 MGI level and above there were 16.6 percent of the returns claiming education expense deductions compared to 13.9 percent with dependents but not claiming the education deduction.

A contingency table analysis[1] comparing deduction claimers and non-deduction claimers across the 20 MGI stratification categories having a Chi square of 5230 with 19 degrees of freedom yielded similar results. Comparison of expected numbers of returns with observed values indicated that for all MGI stratifications below $20,000, observed values were less than expected values for those claiming deductions and greater than expected values for those not claiming deductions. The reverse was true

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[1] Statistical test not necessary with population data, but presented for descriptive purposes.

for all returns falling in MGI stratification categories of $20,000 and above. The break-off point appears to be close to $20,000 MGI, indicating that returns claiming the dependent education deduction tend to be somewhat more associated with higher income levels than returns with dependents but not claiming the deduction.

Data used to address Research Question #3 are presented in Table 5. The state of Minnesota is divided into 9 educational cooperative service units (ECSUs) which were convenient frames for analysis. The only major problem with the ECSU frame was that ECSU 11, which included the Twin Cities Metropolitan area, contained most of the population, income, non-public schools and enrollments.

The data in the columns of Table 5 were converted to ranks for each ECSU. Observation of the rank orders (see Table 6) indicated a generally positive relationship among all the variables. To summarize these relationships, rank order correlations were computed between the MGI/return ranks and each of the non-public school ranks. Similarly, rank order correlations were computed between returns claiming the education deduction and each of the non-public school rankings. The correlations are presented in Table 7.

The rankings of percent non-public schools, percent non-public enrollments, and percent non-public enrollment of total enrollments were positively related to MGI/return (Spearman Rho of .66, .73, and .43, respectively). Positive correlations were also found between the percent returns claiming education deductions and the percent non-public schools

Table 5

Estimated Population Data on Returns Claiming Education Deductions and Minnesota Gross Income and Non-Public Average Daily Membership (ADM), Percent Non-Public of Total ADM and Non-Public Schools by Educational Cooperative Service Region (ECSU) During 1980

ECSU	Deductions Claimed		Minnesota Gross Income/Return[a]	Non-public Enrollment[b]		Percent Non-public of Total[b]	Non-public Schools[b]	
	Number	Percent	Amount	Number	Percent		Number	Percent
Unknown	1	0	7,025	--	--	--	--	--
1	1,538	1.79	12 029	1,984	2.18	5.43	20	3.68
3	10,088	11.76	16,570	2,858	3.14	4.00	27	4.96
4	3,023	3.53	13,048	2,117	2.33	5.39	19	3.49
5	2,377	2.76	11,864	2,204	2.42	7.33	20	3.68
6	4,194	4.88	13,912	5,871	6.45	8.88	58	10.66
7	5,331	6.21	14,746	7,887	8.67	10.04	53	9.74
9	2,728	3.17	15,212	6,386	7.02	14.20	50	9.19
10	6,681	7.78	15,075	8,898	9.79	10.38	66	12.13
11	49,847	58.12	19,534	52,749	58.00	12.91	231	42.47
Total	85,748	100	16,882	90,954	100	10.56	544	100

a. Source: Minnesota Department of Revenue

b. Source: Compiled from reports prepared by the Minnesota Department of Education

Table 6

Ranking by ECSU

ECSU	Non-public Schools	Non-public Enrollments	Non-public % of Total Enrollment	Returns with Deduction	MGI/Return
1	7.5	9	7	8	8
3	6	6	9	3	2
4	9	8	8	7	7
5	7.5	7	6	9	9
6	3	5	5	4	6
7	4	3	4	5	5
9	5	4	1	6	3
10	2	2	3	2	4
11	1	1	2	1	1

Table 7

Rank Order Correlation Coefficients

		Non-public Schools	Non-public Enrollments	Non-public % of Total Enrollment
MGI/return ($r_s = .85$, $r_t = .83$)	Spearman (r_s)	.66*	.73*	.43
	Kendall Tau (r_t)	.42	.56	.39
	Partial Tau	-.17	.21	.34
Returns with Deductions	Spearman	.84*	.80*	.37
	Kendall Tau	.70	.61	.22
	Partial Tau	.64	.37	-.09

*significant at .05 level

and percent non-public enrollments (Spearman Rho of .84 and .80, respectively). The Spearman rank order correlation between MGI/return and percent returns claiming education deduction across the 9 ECSU regions was .85. Although it is difficult to separate the compounding that might exist in these relationships with the distributions of population and resources across the ECSU regions, this evidence indicates that there was at least a moderate relationship between availability of non-public education and enrollments with both income and claiming of the deduction.

The Kendall Taus in Table 7 are, as usual, more conservative than the Spearman rank order correlation coefficients. They were useful, because they allowed computation of partial Taus (analogous to partial correlation coefficients) also reported in Table 7. Partial Taus in the row labeled MGI/returns are controlled by returns with deductions. Partial Taus in the row labeled returns with deduction are, in turn, controlled by percent MGI. The partial correlations indicating relationship between percent returns with deductions and non-public schools changes very little when MGI is controlled. The relationship between returns with deduction and non-public enrollment as a percent of total enrollment is still weak, but also changes direction and becomes negative when MGI/return is controlled. When the partial Taus correlating MGI/return with the three non-public education variables were computed, two of them (non-public schools and non-public enrollments) decreased whereas the third (non-public enrollment as percent of total enrollment) remained relatively weak but constant when returns with deductions was controlled. These data indicate that, in general, there is some degree of relationship between claiming the dependent education deductions and the availability of non-public instruction, even when wealth is controlled.

Summary Discussion

The results reported are summarized and interpreted as follows:

1) Department of Revenue information relative to the impact of M.S. 290.09 Subdivision 22 is limited to statistics describing dependent education expense deductions by MGI stratification and state totals, estimates of forgone income tax revenue, and distribution of deductions by size. Confidentiality of the data limits access for research purposes to the Department.

2) Fiscal impact of M.S. 290.09 Subdivision 22 appears relatively minor compared with total state allocations for elementary/secondary education. A small but growing number of returns itemizing deductions are claiming dependent educational expenses. In 1978, 33,050 returns or 1.9 percent of itemized returns resulted in an estimated $2,466,000 reduction in state income tax revenue. In 1980, 86,180 returns or 4.9 percent of itemized returns resulted in an estimated $4,095,000 reduction in state income tax revenue. Increased statutory deduction allowances, fee for service trends in public schools, and broader coverage of the statute could result in greater fiscal impact.

3) With the risks of generalizing from only two points in time, different populations appeared to be taking advantage of the provision in 1978 and 1980. In 1978, 50 percent of the tax returns had deductions of $500 or less. In 1980, 50 percent of the returns had deductions of $200 or less. This change suggests that more public school parents whose deductions must be limited to fees or other non-tuition and transportation expenses were taking advantage of the law. The mean of 2.71 dependent per return in 1978 compared to 2.38 in 1980 suggests that a greater proportion of small families were taking advantage of the law.

4) Caution is necessary in making educational policy inferences from Department of Revenue data. Dependents providing the bases for education expense deductions are listed on returns with itemized deductions; numbers of returns from parent/filers with school-age dependents not itemizing deductions are unknown. The proportion of dependent expenses claimed that were incurred in non-public vs public schools is unknown. The comparison group of returns itemizing deductions, claiming dependents, but not making dependent education expense deductions cannot be regarded as a control group. The extent to which it represents parent/filers who itemize deductions with children in "free" public schools is uncertain because it was not possible to partial out returns in which dependents claimed were not school-age children, comparisons between the groups assumed that the proportion of claimed dependents who are school-age children was unrelated to other variables being considered. Within these limitations, returns claiming dependent education deductions tended to fall in somewhat higher MGI brackets than returns with dependents but not claiming education expense deductions.

5) Participation in private education is a function of the availability of those facilities/opportunities. Place of residence, particularly near a metropolitan area, determines a parent/filer's opportunity to take advantage of private education and claim expense deductions under the law. This remains true to a reduced extent, when wealth is controlled.

6) The Spearman rank order correlation between MGI/return and claiming deductions was .85, with a Tau of .83 (See Table 7). When the Tau is "partialed" to control for the three measures of non-public school availability a partial Tau of .75 is achieved. This indicates that a

relatively strong relationship between income and claiming the deduction (see research question 2) remains strong even when the availability of non-public education varies.

7) Department of Revenue data appear to provide no direct evidence on the issues at trial in Mueller vs Allen. The available data provide no indication of a) what objects of expenditure the deductions actually pay for in either public or non-public elementary/secondary education, b) what institutional benefits public or non-public schools receive as a result of the deduction, or c) relative benefits to tax payer-parents of public school vs, non-public school children. Data addressing these issues would have to be collected in a further study.

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